

ANALYSIS OF ORIGINAL BILL

Author: Senate Revenue & Taxation Committee Analyst: Nicole Kwon Bill Number: SB 1044
 Related Bills: See Legislative History Telephone: 845-7800 Introduced Date: March 14, 2007
 Attorney: Douglas Powers Sponsor: _____

SUBJECT: Disallowance Of Deduction If Failure To Report Payments For Personal Services/Technical Clean-Up

SUMMARY

This bill would amend Revenue & Taxation Code (R&TC) sections 17299.8, 19175, and 24447 to eliminate repealed cross-references and instead refer to current section 18631.

PURPOSE OF THE BILL

The purpose of this Franchise Tax Board (FTB)-sponsored bill is to remove any ambiguity regarding the authority of FTB to disallow deductions for unreported payments made for personal services, thereby eliminating possible disputes between taxpayers and the department.

EFFECTIVE/OPERATIVE DATE

This bill would be effective and operative for taxable years beginning on or after January 1, 2008.

POSITION

Support.

On December 4, 2006, the Franchise Tax Board voted 2-0, with the member from the Department of Finance abstaining, to sponsor the language included in this bill.

ANALYSISSTATE LAW

Existing state law provides that FTB may disallow a deduction for payments made to an individual or entity as remuneration for personal services if those payments are not reported on Forms W-2 (Wage and Tax Statement) and 1099 (payment reporting) as required and as further described under Background. In addition, current state law imposes a penalty if any person or entity fails to report amounts paid as remuneration for personal services.

Board Position:

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Department Director

Date

Selvi Stanislaus

4/9/07

THIS BILL

This bill would amend R&TC sections 17299.8, 19175, and 24447 to refer to current section 18631 instead of repealed code sections 18637 and 18638.

IMPLEMENTATION CONSIDERATIONS

Implementation of this proposal would not significantly impact the department.

BACKGROUND

California law generally follows federal law by requiring businesses to file information returns reporting payments made by or to other persons (Forms W-2 and 1099). This information is matched against income tax returns and generally used for purposes of identifying taxpayers that have underreported or failed to report corresponding amounts received as income and to verify certain deductions.

The provision disallowing a deduction if the taxpayer failed to file information returns was enacted as part of the original California tax amnesty legislation in 1984 and was amended a few years later to make the provision discretionary rather than mandatory in its application.

AB 2892 (Assembly Committee on Revenue & Taxation, Stats. 2000, Ch. 863) added, amended, renumbered, and repealed various sections of the R&TC to conform more closely to the language and structure of the Internal Revenue Code.

OTHER STATES' INFORMATION

The states surveyed include *Illinois*, *Massachusetts*, *Michigan*, *Minnesota*, and *New York*. These states were selected due to their similarities to California's economy, business entity types, and tax laws. The states of *Illinois*, *Massachusetts*, and *New York* have the same provisions as California. It is unclear if *Michigan* and *Minnesota* have this same provision.

FISCAL IMPACT

This bill would not impact the department's costs.

ECONOMIC IMPACT

This bill would not impact the state's income tax revenue because this bill merely clarifies existing law by resolving an ambiguity.

LEGISLATIVE STAFF CONTACT

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